

# **PUBLIC REPORT**

Ombudsman Complaints A2006-0166, 0195 & 0196 (Finding of Record and Closure)

June 29, 2007

(Edited to remove confidential information per AS 24.55.160)

#### **SUMMARY OF THE COMPLAINT**

At the beginning of February 2006, the Office of the Ombudsman received three complaints against the Office of Economic Development (OED), which is an agency of the Alaska Department of Commerce, Community, and Economic Development (DCCED). Washington residents Richard Blanc, Lanny Carpenter, and Erick Sabo (Complainants) complained that OED discriminated against them. Specifically, they alleged that OED denied them grants under the Southeast Alaska Salmon Vessel Quality Upgrade Program (SAVQUP) because they were not Alaska residents.

After an initial review of the complaint, the ombudsman opened an investigation into the following allegation stated in terms to conform with AS 24.55.150, which authorizes the ombudsman to investigate complaints about administrative acts of state agencies:

Contrary to law: The Alaska Office of Economic Development discriminated against non-Alaska residents applying for grants from its Salmon Vessel Quality Upgrade Program.

The ombudsman finds this allegation *justified* for the reasons set forth in this report.

Assistant Ombudsman David Newman investigated the allegations and forwarded his report to the ombudsman. Mr. Newman gave written notice of the investigation to Fisheries Development Specialist Glenn Haight on October 20, 2006 in accordance with AS 24.55.140.

## **BACKGROUND**

In 2003, the State of Alaska implemented the Fisheries Revitalization Strategy (Strategy). The Strategy is an economic development program designed to increase innovation and productivity in the depressed Alaska salmon industry. According to the SAVQUP application, "It is generally accepted that a primary contributing factor to this decline is the rapid increase in farmed salmon production."

The Strategy combined \$35 million in federal disaster funding with \$15 million in federal Southeast Sustainable Salmon Fund monies. The \$35 million in disaster funding was authorized under Title 5, Section 501(b) of the 2003 Federal Appropriations Bill. It states in part:

... \$35,000,000 shall be made available as direct lump sum payment to the State of Alaska no later than 30 days after the date of enactment of this Act to make payments to persons or entities which have experienced significant economic hardship. Funds in Alaska shall be used to provide: ... (ii) assistance for small businesses including fisherman, fish processors, and related businesses serving the fishing industry...

The \$15 million in Southeast Sustainable Salmon Fund monies was authorized under Title VI, Section 628(d)(2)(A) of the Pacific Coastal Salmon Recovery Fund. It states:

For salmon habitat restoration, salmon stock enhancement, and salmon research, including the construction of salmon research and related facilities, there is authorized to be appropriated for each of fiscal years 2000, 2001, 2002, and 2003, \$90,000,000 to the States of Alaska, Washington, Oregon, and California. Amounts appropriated pursuant to this subparagraph shall be made available as direct payments. The State of Alaska may allocate a portion of any funds it receives under this subsection to eligible activities outside Alaska.

An important part of the Strategy is the Targeted Fisheries Assistance Program (TFAP). The TFAP was intended to supplement prior grant programs by providing grant assistance aimed at solving development problems facing distressed salmon fisheries.

As a part of the TFAP, the Salmon Vessel Quality Upgrade Program (SAVQUP) funded upgrades to active salmon fishing boats and tender vessels. SAVQUP made available \$1 million in grant funds, and each applicant could seek an award of up to \$25,000. Eligibility was limited to:

- (1) For-profit business[es] that meet the U.S. Small Business Administration's definition of a small business as defined by the SBA's Office of Size Standards ... and that hold a:
- (a) limited entry salmon permit from Commercial Fisheries Entry Commission that was fished during the last three salmon seasons, or

(b) tender vessel permit from Commercial Fisheries Entry Commission and can demonstrate significant salmon tendering activity during the last three salmon seasons.

According to a December 23, 2005, press release on the SAVQUP program:

Eligible projects include: freezers; coolers; ice machines, chutes, and accessories; hold insulation and related repairs; refrigerated sea water systems; slush bags; generators or generator upgrades related to quality improvement equipment; quality handling equipment and/or the fabrication of quality handling equipment; and insulated totes for use on the vessel.

## **INVESTIGATION**

OED started accepting applications for the SAVQUP grant on January 1, 2006. The application was divided into five scoring sections, with 100 total points possible. Applicants receiving a score of at least 70 points were eligible to receive funding. The five sections and point allocations were as follows:

- <u>Eligible Applicant</u>: Scores will be based upon the ability of the applicant to execute the project and the applicant's knowledge of or experience with other similar projects. (15 points)
- <u>Community/Industry Sectors Served</u>: Scores will be based on the degree of impact from the downturn in the salmon fishing industry on the community(ies) from which the applicant operates its fishing operations during the salmon season and the community(ies) in which the project will take place. (30 points)
- <u>Project Description</u>: Scores will be based on the degree of impact increases in profitability . . . the project will have on the communities impacted by the downturn in the salmon fishing industry. (35 points)
- <u>Budget</u>: Scores will be based upon the applicant's appropriate use of the budget form provided in the application and ability to provide a cash match for at least 50 percent of the budget. (10 points)
- <u>Long-Term Value</u>: Scores will be based upon the project's ability to increase product quality and ex-vessel<sup>1</sup> price. (10 points)

The application then went on to state that:

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<sup>&</sup>lt;sup>1</sup> The ex-vessel price table is an index of changes in the relative dockside value of fish and shellfish sold by fishing vessels. The table indexes the average annual ex-vessel price (price per pound) received for each species or group to the average price per pound received for the same species or group in the base year.

Scores will be forwarded to the Commissioners of Fish & Game and Labor & Workforce Development or their designees and to the Fisheries Policy Advisor in the Office of the Governor...

During January 2006, the Complainants submitted their applications to OED. Mr. Sabo applied for two grants totaling \$3,431. He intended to use the grant money to install slush ice bags on his two boats. Mr. Blanc and Mr. Carpenter applied for one grant each, totaling \$24,690 and \$25,000 respectively. They intended to install refrigerated sea water systems on their boats. Mr. Sabo and Mr. Carpenter fished primarily in Bristol Bay while Mr. Blanc fished primarily in Kodiak.

After OED's initial scoring, the Complainants each failed to qualify for the grant. The primary reason for their failure to reach the 70-point threshold was that they each received a score of 1 out of 35 in the "Project Description" section.

The following chart lists the Complainants, their requested grant amounts, and the points awarded in the various categories. The following chart only shows results with regard to the Complainants. It does not show the other applicants. After OED's initial scoring, the results were as follows:

Applicant	Requested Amount	Eligible Applicant (15)	Community/ Industry Sector Served (30)	Project Description (35)	Budget/ Match (10)	Long- Term Value (10)	Total (100)	Award
Richard Blanc	\$24,690	15	27	1	10	10	63	\$0
Lanny Carpenter	\$25,000	15	30	1	10	10	66	\$0
Erick Sabo	\$1,468	15	30	1	10	10	66	\$0
Erick Sabo	\$1,963	15	30	1	10	10	66	\$0

According to a spreadsheet provided by OED to the Complainants, there were 56 applications for SAVQUP grants. Of the 56 applications, 27 applications listed Bristol Bay and Kodiak as their primary fishing region. Of those 27 applications, 17 were from an applicant with an Alaska resident address, while 10 were from residents of Washington or Oregon. After the initial scoring, all 17 Alaska residents received grant funding. All 10 of the residents of Washington and Oregon received nothing.

After being informed of their failure to qualify for the grant, the Complainants filed a Request for Reconsideration with then-DCCED Commissioner William Noll. Commissioner Noll did not immediately respond to their requests. On February 21, 2006, the ombudsman investigator contacted OED grants administrator Debbie McBride. The investigator asked Ms. McBride if the Complainants would be receiving a response from

Commissioner Noll. Ms. McBride responded that OED was coordinating with the commissioner's office to get a response to the Complainants as soon as possible.

The next day, the investigator e-mailed Ms. McBride with a follow-up question to their phone conversation. The investigator asked Ms. McBride why the Complainants only received a score of 1 point in the Project Description section. The investigator wrote:

Why were the out-of-staters only given a 1/35 in the [Project Description] section if they live in those AK communities at least 4 months out of the year? Were the four months not counted?

# Ms. McBride responded:

The [Community/ Industry Sector Served] section deals with where the person fishes from during the fishing season and where the project will take place. The [Project Description] section deals with where the fishermen spends his money the rest of the year, which is typically at least 2/3rds of the year, often more for certain fisheries.

The following day, Ms. McBride informed the investigator that the Department of Law was reviewing the reconsideration requests.

On April 24, 2006, OED Program Manager Glenn Haight provided the investigator copies of letters that were sent to the Complainants. The letters informed the Complainants that based on its discussion with the Department of Law, OED would rescore their applications if they provided additional information about how they spent their profits in communities impacted by the downturn in the Alaska salmon industry. Mr. Haight wrote:

Following scoring of the SAVQUP applications, the Department received a number of responses from applicants based on the Department's determination of whether profits from the applicant's project would likely be spent in the communities significantly impacted by the downturn in the salmon industry. With the help of those responses and advice by the Department of Law, the Department determined it is appropriate to seek additional information and re-score the applications that provide this additional information.

OED gave the Complainants 20 working days to respond. All responded within the deadline.

The ombudsman later learned that Assistant Attorney General Chris Poag was advising OED on this matter. The ombudsman asked OED to provide copies of all the correspondence between itself and the Department of Law, but OED refused, claiming

attorney-client privilege and Ombudsman Statute 24.55.160(a)(4) and 24.55.330(3).<sup>2</sup> The Ombudsman officially asked then-Commissioner Noll to waive the privilege but he declined, citing advice from the Department of Law.

On June 22, 2006, Ms. McBride sent an e-mail to the Commissioners of DCCED, Fish & Game, and Labor & Workforce Development, and to the Fisheries Policy Advisor in the Office of the Governor. Together, this four-member group is known as the "Fish Cabinet." According to the Alaska Salmon Marketing Grant Program dated February 2005, the "Fish Cabinet" works "closely together to craft the [State of Alaska's] response to the many challenges facing the salmon industry."

# Ms. McBride wrote:

Following the SAVQUP application review process, the Department received a number of requests for reconsideration from applicants that did not score high enough because they did not spend their profits in a community impacted by the downturn in salmon. This was determined through a review of the Permanent Fund Dividend rosters. Applicants claimed residency discrimination. On the advice of the Department of Law, the Department sought to rescore the applications after seeking additional information about how much of their profits were spent in Alaska and how many months they spent there.

[Language in this paragraph has been removed at the request of DCCED and pursuant to AS 24.55.160(b).] The net result from our rescoring process is the recommended award of 16 additional grants for a total of \$249,021...

The Department is seeking advice from the Fish Cabinet regarding this action.

Because the ombudsman was denied access to the correspondence between the Department of Law and OED, the information about advice from Law cannot be confirmed.

AS 24.55.160 Investigation procedures. (a)

<sup>&</sup>lt;sup>2</sup> AS 24.55.160 Investigation procedures. (a) In an investigation, the ombudsman may: . . . (4) notwithstanding other provisions of law, have access at all times to records of every state agency, including confidential records, except sealed court records, production of which may only be compelled by subpoena, and except for records of active criminal investigations and records that could lead to the identity of confidential police informants.

AS 24.55.330 Definitions. In this chapter . . . (3) "record" means a document, paper, memorandum, book, letter, drawing, map, plat, photo, photographic file, motion picture, film, microfilm, microphotograph, exhibit, magnetic or paper tape, punched card, or other item developed or received under law or in connection with the transaction of official business, but does not include an attorney's work product, material that is confidential as a privileged communication between an attorney and client under ruled adopted by the supreme court, or confidential oil and gas geological and geophysical data. (emphasis added)

On July 11, 2006, Mr. Haight informed the investigator that the new scoring system had been sent to the Fish Cabinet for its review. Mr. Haight then sent the investigator a copy of the new scoring system. As part of OED's rescoring, 19 applicants who submitted additional information were re-evaluated and a total of 16 scored high enough to receive a SAVQUP grant.

The Complainants each scored high enough to receive the grant. The following chart lists the Complainants, their requested grant amount, and the points awarded in the various categories upon reconsideration. Again, the following chart only shows results with regard to the Complainants. It does not show the other applicants.

Applicant	Requested Amount	Eligible Applicant (15)	Community/ Industry Sector Served (30)	Project Description (35)	Budget/ Match (10)	Long- Term Value (10)	Total (100)	Result
Richard Blanc	\$24,690	15	27	15.8	10	10	78	Winner
Lanny Carpenter	\$25,000	15	30	5.8	10	10	71	Winner
Erick Sabo	\$1,468	15	30	5.8	10	10	71	Winner
Erick Sabo	\$1,963	15	30	5.8	10	10	71	Winner

On July 14, the Fish Cabinet met to discuss the rescoring.

After that meeting, Mr. Haight e-mailed the Fish Cabinet and stated:

At the Fish Cabinet meeting of Friday (7/14), the Fish Cabinet commented on the rescoring methodology for previously denied applications under the salmon vessel quality upgrade program to be unsatisfactory in meeting the intent of the SAVQUP program. SAVQUP was designed to maximize the impact of grant funds to those areas significantly impacted by the downturn in the salmon industry. The Fish Cabinet found that the rescoring process used by the Department was inadequate for the purpose of significantly benefiting those communities impacted by the downturn in the salmon industry.

The Department is prepared to incorporate the Fish Cabinet's recommendations and not fund the rescored applications.

Please let me know if you have any further input in this matter.

Fisheries Policy Advisor Alan Austerman responded to Mr. Haight in an e-mail stating that "You are correct, the Fish Cabinet decided the rescoring process did not meet the original intent of the SAVQUP program."

On August 14, 2006, Mr. Haight wrote to the Complainants and informed them their applications had been denied. Mr. Haight stated:

The Department of Commerce, Community & Economic Development completed its review of your application under the TFAP: SAVQUP grant program. The application rescoring performed by the Department was found insufficient by the Fish Cabinet to assure the project would measurably improve the economic situation of those communities impacted by the downturn in the salmon industry. Based on the Fish Cabinet's comments, the Department's scores have been modified and your application is denied.

On August 15, 2006, Mr. Haight informed the investigator of OED's decision. The ombudsman was unable to verify this account of the Fish Cabinet meeting as there were no notes or minutes taken at the meeting.

# **ANALYSIS AND PRELIMINARY FINDING**

The standard used to evaluate all ombudsman complaints is the **preponderance of the evidence**. If the preponderance of the evidence indicates that the administrative act took place and the complainant's criticism of it is valid, the allegation is found justified.

In this case, the ombudsman investigated whether OED discriminated against non-Alaska residents applying for grants from the SAVQUP in a manner contrary to law.

The Office of the Ombudsman's Policies and Procedures Manual at 4040(1) defines *contrary to law*. The portion of the definition relevant to the allegation is:

(A) Failure to comply with statutory or regulatory requirements.

\* \* \* \* \*

The Alaska Fisheries Revitalization Strategy was funded by two federal measures: federal disaster appropriations included in the 2003 Federal Fiscal Year budget and the Southeast Sustainable Salmon Fund. Those two pots of money were combined to fund the Alaska Fisheries Revitalization Strategy.

Language in the 2003 Federal Appropriations Bill directed that \$35 million be granted to the State of Alaska to make payments to persons or entities which have experienced significant economic hardship. Such funds in Alaska shall be used to provide, among other things:

(ii) assistance for small businesses including fisherman, fish processors, and related businesses serving the fishing industry...

Language in the Pacific Coastal Salmon Recovery Fund, (Title VI, Section 628(d)(2)(A)) which funded the Southeast Sustainable Salmon Fund states the Fund's purpose as:

For salmon habitat restoration, salmon stock enhancement, and salmon research, including the construction of salmon research and related facilities, there is authorized to be appropriated for each of fiscal years 2000, 2001, 2002, and 2003, \$90,000,000 to the States of Alaska, Washington, Oregon, and California. Amounts appropriated pursuant to this subparagraph shall be made available as direct payments. **The State of Alaska may allocate a portion of any funds it receives under this subsection to eligible activities outside Alaska.** [Emphasis added]

The grant language for these funds did not direct that fund distribution be limited only to Alaska residents. The purpose of the allocations was to improve the wild salmon industry, which, according to the Alaska Fisheries Revitalization Strategy, was suffering a decline because of the rapid increase in farmed salmon production. The Complainants, despite their legal residency, were and are part of the Alaska salmon industry. On its face, the work they did on their vessels fulfilled the criteria to receive the grant.

Article IV, Section 2 of the U.S. Constitution states "The Citizens of each State shall be entitled to all Privileges and Immunities of Citizens in the several States." In *Toomer v. Witsell*, 334 U.S. 385 (1948), the Court stated that the Clause bars "discrimination against citizens of other States where there is no substantial reason for the discrimination beyond the mere fact they are citizens of other states."

In *Hicklin v. Orbeck*, 437 U.S. 518 (1978), the Court reviewed the Local Hire Under State Leases statute (AS 38.40.010 to 38.40.090 (1977)), otherwise known as "Alaska Hire," which gave Alaska residents a preference for jobs in the state's oil industry. Alaska Hire was passed in order to help reduce unemployment in the state. In *Hicklin*, the Court used a two-part test to determine if Alaska Hire violated the Privileges and Immunities Clause. First, the Court reviewed whether non-residents were a "peculiar source of the evil" that the statute was enacted to remedy. Second, the Court reviewed whether the discrimination against non-residents bore a "substantial relationship" to the problem the statute was intended to solve. The Court unanimously struck down the statute, finding that there was no substantial relationship between Alaska's unemployment problem and the "evil" that the non-residents were said to present.

In this case, OED denied the Complainants' applications because they failed to meet a minimum score of 70. However, it would have been mathematically impossible for the Complainants, along with the other fisherman who listed their primary residence as Washington and Oregon, to reach the 70 point threshold because, as non-residents, they automatically received a score of 1 out of 35 in the Project Description section. As non-residents, the maximum points they all could receive was 66.

By making it mathematically impossible for the Complainants and other non-residents to receive the SAVQUP grant, OED discriminated against the Complainants solely based on their non-Alaska residency. In order to dispel the claims of discrimination and meet the

burden set forth in *Hicklin*, OED would have to prove that the Complainants were a "peculiar source of the evil" and that the discrimination bore a substantial relationship to the problem that the SAVQUP was intended to solve.

The OED is unable to meet the burden in *Hicklin*. First, the Complainants cannot be considered a "peculiar source of the evil" because, according to the State's own Fisheries Revitalization Strategy, they were not and are not a primary contributing factor to the downturn in the Alaska salmon industry.

According to the SAVQUP application guide, "It is generally accepted that a primary contributing factor to this decline *is the rapid increase in farmed salmon production*." Moreover, even if OED could somehow show that the Complainants were a "peculiar source of the evil," the discrimination against the Complainants is still unacceptable because it does not bear a substantial relationship to the problem the SAVQUP intended to solve. In fact, the opposite appears to be true. The money that the Complainants spend during their time in Kodiak and Bristol Bay creates a direct fiscal benefit to those regions. In addition, the slush ice bags and refrigerated sea water system improvements that the SAVQUP grant would provide to the Complainants' boats presumably would improve the quality of the products being produced and sold in Alaska and thus improve the industry.

Based on the facts of this case and the precedent set in *Hicklin*, the ombudsman believes that OED has discriminated against the Complainants in violation of the Privileges and Immunities Clause of the U.S. Constitution. Therefore, the ombudsman finds that OED acted contrary to law and that the allegations of the Complainants are *justified*.

## **Agency Response**

On May 7, 2007, DCCED Commissioner Emil Notti responded on behalf of OED to the ombudsman's Preliminary Report. (Commissioner Notti was not in office when the events documented in this report occurred.) The Preliminary Report stated, "Based on the facts of this case and the precedent set in *Hicklin*, the ombudsman believes that OED has discriminated against the Complainant's in violation of the Privileges and Immunities Clause of the U.S. Constitution." In response to this finding, Commissioner Notti stated that:

The Department does not support this finding and believes that it is unnecessary for resolution of this matter. The Department agrees that the scoring system initially used did not comport with the terms of the grant at issue. This is confirmed by the preliminary report which at page 9 states correctly that: "The grant language for these funds did not direct the fund distribution be limited only to Alaska residents."

Further the preliminary report at page 4 finds that the first scoring system was set up so that no out of state residents could reach the needed 70

threshold because they were awarded 1 point out of 35 under the criteria "[Project Description]."

Taken in tandem, these two findings in the preliminary report support the first two recommendations made by your office and are sufficient to find that OED did not follow the law and that the special assessment criteria "should be adjusted..."

The Hicklin case at pp. 524-526 held that the Privileges and Immunities Clause "does not preclude disparity of treatment in the many situations where there are perfectly valid independent reasons for it, nor does it "bar discrimination against citizens of other States where there is no reason for the discrimination beyond the mere fact that they are citizens of other States," citing Toomer v. Witsell, 334 U.S. 385, 396 (1948). See also Mullaney v. Anderson, 342 U.S. 415 (1952).

Indeed, Justice Brennan noted that there may be circumstances in which a preferential hire system enacted by a state could pass Constitutional muster. The problem for Alaska in Hicklin was that their criteria were not present. Justice Brennan noted that a state might be justified in restricting employment to residents if an influx of nonresidents were the reason for the employment problem. However, Alaska's high unemployment at the time of the Court's decision was not directly related to nonresidents coming in and taking jobs away from local people. Rather, according to a report by the Federal Field Committee for Development Planning in Alaska the state's unemployment problem was a result of local conditions because "[t]hose who need the jobs the most tend to undereducated, untrained, or living in areas of the state remote from job opportunities."

The Privileges and Immunities Clause has been held to prohibit state durational residency requirements such as those in the Hicklin case itself or more recently in Saenz v. Roe, 526 U.S. 489 (1999) with respect to welfare payments. However, it is questionable that it would be applied to grant administration where there may be valid reasons for intra-state and inter-state distinctions.

Given the report's overall recommendations, with which the Department agrees, the correct conclusion here is that the grants were not meant to be limited to Alaskan residents. It is uncontroverted that the initial scoring system worked to eliminate all non-residents so that there is a sufficient basis in this record for the first two recommendations made by your office. We would therefore respectfully request that the legal discussion of Hicklin at pp. 9 and 10 of the preliminary findings be removed.

## **Ombudsman Response:**

The ombudsman disagrees with Commissioner Notti's statement that "it is questionable that [the Privileges and Immunities Clause] would be applied to grant administration where there may be valid reasons for intra-state and inter-state distinctions." As the ombudsman previously stated, there was no valid reason in this case for making a distinction between in-state and out-of-state residents. Therefore, the ombudsman will not remove the legal discussion of Hicklin from this section.

# PROPOSED RECOMMENDATIONS

In this case, the ombudsman believes that OED acted contrary to law by discriminating against non-Alaska residents. Therefore, the ombudsman proposes the following recommendation:

#### Recommendation 1

OED should accept all of the rescored applications that met the minimum score of 70. OED should then pay out the grant funds to all of the applicants who qualified.

OED agreed with this recommendation.

#### Recommendation 2

The 2007 SAVQUP application assessment criteria should be adjusted to eliminate the discriminatory scoring. [Additional language in this paragraph has been removed pursuant to AS 24.55.160(b).]

#### Commissioner Notti responded:

OED has already responded to the recommendation by writing a certified letter to the 16 applicants advising them that the department has reevaluated their application under the Alaska Salmon Vessel Quality Upgrade Program (SAVQUP) and have found that they are now eligible to receive and award. Further, we have reserved funds in the amount of \$249,021 from various programs within the grant to award the new 16 eligible applicants. [Language in this paragraph has been removed pursuant to AS 24.55.160(b).]

#### Recommendation 3

Governmental decisions that affect individuals' livelihood should not take place in a vacuum. Future meetings of the "Fish Cabinet" should be documented in some form, whether it be by a secretary taking notes or a Board secretary taking minutes.

The applications for 2007 have been published and some of the criteria has been changed. The effect of this is that the Complainants are no longer eligible for funds because the fishing areas are limited to a Southeast or Yakutat fishery. If the assessment scoring scale remains the same, the discrimination will continue. This scoring should be amended at the least to reflect the scale proposed by the Department of Law.

# Commissioner Notti responded:

The department agrees that any committee of state officials making decisions on grant applications should prepare meeting minutes and should document their decision process with respect to grant awards. Furthermore, this department is committed to transparency and will adhere to the Open Meetings Act for all meetings to which that Act applies. The department concurs that important decisions should be documented.

Commissioner Notti then added, "Please be advised that the aforementioned recommendations will be implemented immediately."

#### FINDING OF RECORD AND CLOSURE

Based on OED's decision to comply with all three recommendations, the ombudsman closed this complaint as *justified* and *rectified*.